TESTIMONY OF
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NATIONAL ASSOCIATION OF SECURITIES PROFESSIONALS

BEFORE THE
SENIOR HEALTH SECURITY AND RETIREMENT COMMITTEE
OF THE
MICHIGAN HOUSE OF REPRESENTATIVES

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Good Afternoon Chairman Neumann and members of the committee. Thank you for inviting me to provide testimony before you today. I would also like to thank Representative Shanelle Jackson who sponsored House Bill 5618.

I am Donna Sims Wilson, a Member of the Board of Directors and Chair of the National Legislative Committee of the National Association of Securities Professionals (NASP). I am also President of M.R. Beal & Company, a minority-owned investment banking firm in its 22nd year of operation.

I appreciate the opportunity to testify on behalf of NASP and our members concerning our organization's long-standing commitment to promoting the use of emerging managers and emerging broker dealers within all facets of the securities industry and the U.S. capital markets. We commend the committee for recognizing how important this topic is to the future of our economy, our markets, and our industry.

Initially, I will briefly summarize the background and recent legislative initiatives of NASP. I will then focus my testimony on the business imperative for emerging manager and emerging broker programs in the management of public pension plan assets.

BACKGROUND & HISTORY OF NASP

The National Association of Securities Professionals (NASP) is an organization that supports people of color and women in leveling the playing field in the financial services industry. We connect members to industry leaders and business opportunities; advocate for policies that create equal representation and inclusion; provide educational opportunities; and work to build awareness about the value of ensuring that people of color and women are included in all aspects of the financial services industry. Founded in 1985, NASP is based in Washington, D.C. with 10 chapters in major financial centers throughout the United States including Detroit, Michigan. Our members include asset managers, broker-dealers, pension fund consultants, public finance professionals, investment bankers, securities/bond counsel, commercial bank underwriters, institutional investors, plan sponsors and other professionals in the financial services industry.

Annual Pension Fund & Financial Services Conference

The NASP Annual Pension Fund & Financial Services Conference annually attracts the most senior minority and women professionals who come to seek out future business opportunities. Plan sponsors and allied government professionals also attend in order to take advantage of the training and professional development programs. For the past 20 years, this conference has evolved into one of the nation's largest gatherings of successful minority and women professionals engaged in all facets of the financial services industry. This impressive group of finance professionals includes corporate treasurers, public and corporate plan trustees, broker-dealers, asset management and pension consulting firms, and world-recognized economists. For example, our 2009 annual conference was supported by the following partners and sponsors: M. R. Beal & Company, Citi, Edwards Angell Palmer & Dodge, LLP, Barclays Capital, Invesco, Lewis & Munday, PC, Northern Trust Company, Piedmont Investment Advisors, Bank of NY Mellon, Capri Capital Partners, LLC, EARNEST Partners, J.P.Morgan, Mesirow Financial among many other financial services firms.

Legislative Committee & Symposia

In furthering NASP's goal of being a voice for minorities and women to the executive, legislative and regulatory branches of government, we actively engage in legislative initiatives. Since 2005, our legislative committee has testified before the United States Congress several times on topics including both supplier and workforce diversity in the financial services industry, the use of emerging managers and emerging brokers with the $240 billion Federal Retirement Thrift, a public pension plan for U.S. government employees and most recently systemic risk and regulatory reform of our nation's capital markets in the wake of our economic crisis. We have been successful in drafting language that became law, specifically Section 107b of the Emergency Economic Stabilization Act of 2008, otherwise known as the TARP legislation and Section 1116 of the Housing Economic Recovery Act of 2008. Both laws address the issue of the utilization of minority and women owned financial services firms with Federal Government Departments and Agencies including the United States Treasury Department, Fannie Mae, Freddie Mac and the Federal Home Loan Banks among other entities. At the state level, our local chapters have been active in enacting laws in Illinois and Texas that pertain to the use of emerging managers and emerging broker dealers with public pension plans in those states. Just yesterday in Albany, New York, I was priviledged to participate with many NASP members as part of a coalition lobbying for the passage of a bill requiring the use of emerging managers and emerging broker dealers with all public pension plans and departments of the State of New York.

Who Are Emerging Managers?

Simply defined, emerging manager is a specialized industry term. Historically the term was synonymous with minority firms but it has evolved. Today, the term identifies promising investment managers who, by virtue of their relatively short firm investment track record and/or relatively small amount of firm or product assets under management, are traditionally overlooked by pension plans and their consultants in the searches that typically determine who manages institutional pension fund assets. In most cases, the industry has looked to total firm size, i. e. assets under management, as the primary definitional criteria for emerging firms. Today, "emerging manager' most often means those firms that are less than $2—3 Billion in assets under management, and that are independently owned (at least 51% of the firm is owned by individuals working in the firm). Many minority-owned asset management firms in our industry fall within this category of "emerging managers" since they have less than the threshold $2—3B in AUM, and are relatively new firms. Thus, "emerging manager" includes, but is not limited to, minority and women-owned firms.

Why Hire Emerging Managers?

Many U. S. plan sponsors invest with emerging mangers in targeted strategies. These strategies are designed to capture emerging manager alpha potential (excess returns above market benchmarks), to access new talent and secure future manager capacity, and to provide more opportunities for newer and smaller firms to diversify the industry.

These large U. S. institutional investors - both corporate plans as well as public plans (states, counties and municipal entities) have committed billions of dollars in assets to targeted emerging manger investment strategies for one reason—they want to win in global capital markets!

With investment firms, size does matter - but not as traditionally perceived. There is a growing body of academic research that supports the fact that small, entrepreneurial investment firms, i. e., emerging managers, can and often do outperform their larger counterparts. See Exhibit 1. In addition to this research, the investment returns of firms like Progress and others in this industry represent solid proof that there's no loss of investment performance or undue risk when using emerging, minority and women-owned investment firms. In fact, one can consistently achieve market-competitive returns through emerging manager investment strategies.

Another reason to hire emerging managers is the diversification they bring to institutional portfolios. The investment management industry is conservative by nature, and slow to change. Despite actual portfolio results and research to the contrary, many institutional investors still perceive bigger as better and, therefore, prefer the large investment firm names that we're all too familiar with instead of seizing the opportunity to hire less well-known small entrepreneurial firms including those asset managers runs by talented minorities and women (many of whom got their initial experiences with larger firms then left to start their own firms). Ironically, the fact is there may well be more unintended risk in those portfolios managed by large firms than investors realize. The huge non-transparent mortgage derivative losses and write-downs suffered by large investment banks, and the demise of Bear Stearns and Lehman Brothers, illustrates the many unknown and unexpected risks in large investment firms.

Finally, hiring emerging managers is a means to not only provide opportunities to new investment talent but also a means to foster new ideas and investment innovation.

Industry "Best Practices" and How Other Large U. S. Pension Plans Use Targeted Emerging Manager Investment Strategies

Exhibit 2 provides a partial list of all of the U. S. pension plans that have utilized targeted emerging manager investment strategies to enhance overall investment returns, diversify their portfolios and reduce manager concentration risk, and provide opportunities for entrepreneurial firms to incubate and deliver new ideas and innovation to the industry -all to benefit the beneficiaries of these plans.

Who Are Emerging Brokers?

Like Emerging Managers, the term Emerging Brokers refers to minority and women owned investment banking firms who participate in the U.S. capital markets as underwriters and/or broker dealers. These firms underwrite the debt of states and municipalities as well as corporations. They are also active underwriters of the equity or stock of major U.S. companies such as Visa, Citigroup and AT&T to name a few of the largest offerings in the U.S. equity capital markets. Most relevant for this committee, however, these firms trade both equity and debt securities with either the internally managed assets of pensions plans or with money managers who are managing assets on behalf of these public plans. This trading is most often accomplished through a directed brokerage program whereby the public plan "directs" their money managers who are managing assets on behalf of the plan to trade a percentage of their commission dollars with minority and women owned firms identified on a list. These percentages range from 10-50% with 25% being the average. Let me be clear that these public plans never direct trading to any one firm, but rather require through their investment policies that their commission goals must be met through one or more firms on their list of approved brokers. These lists vary from plan to plan but usually include at least 20 firms. Some plans such as the Teachers Retirement System of Illinois have over 90 brokers on their list with a 15% directed brokerage goal.

Directed brokerage programs exist because again, like emerging managers, the perception is that a small broker dealer cannot perform to the same level of excellence as well known global firms such as Goldman Sachs, Merrill Lynch or Morgan Stanley. Fortunately, there are third party independent arbiters of trading execution that measure trading performance of all broker dealers. Some of these firms such as Plexus, Abel Noser, QSG, Elkins McSherry and others have rated many emerging brokers highly and have deemed that they add alpha at the trading table. A representative list of public plans that utilize emerging broker programs is attached as Exhibit 3.

A landmark minority brokerage firm survey by Consultiva Internacional clearly showed the level of technological sophistication, years of experience and quality execution offered by these firms is cited below;

- Consultiva Internacional, Inc., *Emerging Brokerage Firms in the U.S.,* Presented to Board of Trustees of the Los Angeles City Employees Retirement System (October 2005)
  (web-address http://www.lacers.org/Investments/News/2005/20051006-EmergingBrokersConference/Emerging%20Brokerage%20Presentation%20-%20Consultiva.ppt).

CONCLUSION

NASP is grateful for the opportunity to add our voice to the discussion of improving opportunities for emerging managers and emerging broker dealers with public pension plans in the State of Michigan. Emerging manager and emerging brokerage programs are numerous through out the United States and have been in existence in some instances for 15 or more years. We stand ready to partner with the Senior Health Security and Retirement Committee, other trade associations, and individual firms to further our stated goal of ensuring that people of color and women are included in all aspects and at all levels of the financial services industry. We strongly urge the swift passage of House Bill 5618.

Thank You.

EXHIBIT 1

BIBLIOGRAPHY OF RESEARCH PAPERS ON EMERGING MANAGERS

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EXHIBIT 2

PARTIAL LIST OF U.S. PLANS USING EMERGING MANAGERS

The following is a representative list of known U.S. Pension Plans that have committed assets to emerging manager strategies:

- **1199SEIU Employees Benefit and Pension Funds**
- **Alameda County Employees' Retirement Association**
- **Arkansas Teacher Retirement System**
- **Bank of America Corporation**
- **Boeing Company**
- **Boulé Foundation**
- **California Public Employees' Retirement System**
- **California State Teachers' Retirement System**
- **Chicago Policemen's Annuity & Benefit Fund**
- **City of Kansas City Employees' Retirement System**
- **City of Philadelphia Board of Pensions and Retirement**
- **Coca Cola Master Retirement Trust**
- **Contra Costa County Employees' Retirement Association**
- **Detroit General Retirement System**
- **District of Columbia Retirement Board**
- **Exelon Corporation**
- **GE Asset Management**
- **Illinois Municipal Retirement Fund**
- **Illinois State Board of Investment**
- **Indiana Public Employees' Retirement Fund**
- **Liberty Mutual Retirement Benefit Plan**
- **Los Angeles City Employees' Retirement System**
- **Los Angeles County Employees Retirement Association**
- **Maryland State Retirement & Pension System**
- **Massachusetts Bay Transportation Authority Retirement Fund**

Exhibit 2 – continued

- Michigan Department of Treasury
- Municipal Employees' Annuity & Benefit Fund of Chicago
- New York City Board of Education Retirement System
- New York City Employees' Retirement Systems
- New York City Fire Department Pension Fund
- New York City Police Pension Fund
- New York State Common Retirement Fund
- New York State Teachers' Retirement System
- Ohio Public Employees Retirement System
- Oregon Public Employees Retirement Fund
- PG&E Corporation
- Pennsylvania Public School Employees' Retirement System
- PPL Services Corporation
- Public School Teachers' Pension & Retirement Fund of Chicago
- San Antonio Fire & Police Pension Fund
- San Francisco City & County Employees' Retirement System
- San Joaquin County Employees' Retirement Association
- Seattle City Employees' Retirement System
- Shell Oil Company
- State of Connecticut Retirement Plans & Trust Funds
- State Universities Retirement System of Illinois
- Teacher Retirement System of Texas
- Teachers' Retirement System of the City of New York
- Teachers' Retirement System of the State of Illinois
- The Pennsylvania Treasury Department
- Verizon Communications, Inc.

EXHIBIT 3

PARTIAL LIST OF U.S. PLANS USING EMERGING BROKER/DEALERS

- Atlanta (GA) Pension Funds
- California Public Employees Retirement System (CALPERS)
- California State Teachers' Retirement System
- Chicago Public School Teachers' Pension Fund
- Chicago Fireman's Annuity & Benefit Fund
- Chicago Municipal Empl. Annuity & Benefit Fund
- Chicago Laborers Empl. Annuity & Benefit Fund
- Chicago Park Employees' Annuity & Benefit Fund
- Chicago Policemen's Annuity & Benefit Fund
- Chicago Transit Authority
- Connecticut Retirement Plans and Trust Funds
- Cook County Annuity and Benefit Funds
- District of Columbia Retirement Board
- Illinois Municipal Retirement Fund
- Illinois State Board of Investment
- Los Angeles City Employees' Retirement System
- Los Angeles Police and Fire
- Maryland State Retirement and Pension System
- Metropolitan Water Reclamation District Retirement Fund
- New York City Employees' Retirement System
- New York City Fire and Police Retirement System
- New York City Retirement System
- New York City Teachers' Retirement System
- New York State Common Retirement Fund
- New York State Teachers' Retirement System
- Ohio Bureau of Workers' Compensation
- Ohio State Teachers' Retirement System
- Philadelphia Board of Pensions and Retirement
- Retirement Board of Allegheny County Pennsylvania
- State of North Carolina, Department of State Treasurer
- State Universities Retirement System of Illinois
- Teachers' Retirement System of the State of Illinois
- Teacher Retirement System of Texas
- Tennessee Consolidated Retirement Board